SAN FRANCISCO PUBLIC LIBRARY
3 1223 06544 6719

City and County of San Francisco

OFFICE OF THE CONTROLLER

WORKERS' COMPENSATION DIVISION OF THE DEPARTMENT OF HUMAN RESOURCES: The Division's Contractor Has Adequate Security for rocessing and Issuing Benefit Checks but the Division and ıe Contractor Should Enhance Some Administrative rocedures

DOCUMENTS DEPT.
NOV 1 0 1999
SAN FRANCISCO
PUBLIC LIBRARY

Audit Number 98101

November 4, 1999

November 4, 1999

Andrea Gourdine, Human Resources Director
Department of Human Resources
44 Gough Street
San Francisco, CA 94103

Dear Ms. Gourdine:

The Controller's Audits Division presents its report concerning the audit of the Workers' Compensation Division's contractor, Foundation Integrated Risk Management Solutions Incorporated (Firm Solutions). The report concludes that Firm Solutions has sufficient security procedures for processing and issuing workers' compensation benefits checks for the City and County of San Francisco (City). However, both the Workers' Compensation Division and Firm Solutions can improve some of the administrative procedures they use in administering the City's workers' compensation program.

The Department of Human Resources' response is attached to this report. The Controller's Audits Division will be working with the Workers' Compensation Division to follow up on the status of the recommendations made in this report.

Respectfully submitted,

EDWARD HARRINGTON
Controller

3 1223 06544 6719

RESULTS IN BRIEF

Our audit of the Workers' Compensation Division (division) of the Department of Human Resources for the City and County of San Francisco (City) revealed that the division's contractor for processing and issuing benefits checks follows sufficient security procedures when handling the checks. However, for the nine months we reviewed, the contractor, Foundation Integrated Risk Management Solutions Incorporated (Firm Solutions), did not prepare monthly bank reconciliations promptly, and its delays prevented the division from correcting discrepancies in the monthly bank statements and identifying early some improper payments of workers' compensation benefits. As a result, the division was late in reviewing the reconciliations and did not discover until summer 1999 that the division and Firm Solutions had incorrectly issued or that the division's bank had improperly paid almost $33,000 in benefits checks from July 1, 1998, through March 31, 1999. One of these improper payments, totaling $13,200, occurred because the division has weaknesses in its practices for handling stop payments on checks.

Also, during January and February 1999, unidentified individuals were able to cash 17 counterfeit checks totaling more than $10,000 on the division's two bank accounts through which it pays workers' compensation benefits. Although the bank paid for the losses, the division can institute a program that will help prevent its bank from honoring counterfeit checks.

Digitized by the Internet Archive
in 2016 with funding from
San Francisco Public Library

https://archive.org/details/workerscompensat4199sanf

INTRODUCTION

The City and County of San Francisco (City), as a self-insured employer, pays workers' compensation benefits to its employees and their dependents for work-related injuries. The City administers its workers' compensation program through the Workers' Compensation Division (division) of the Department of Human Resources. The division administers the workers' compensation program for employees in 30 of the City's 59 departments, as well as employees of the San Francisco Unified School District and the San Francisco Community College District. The division contracts with a private firm, Foundation Integrated Risk Management Solutions Incorporated (Firm Solutions), to administer the workers' compensation program for employees in the remaining 29 City departments. Firm Solutions is also responsible for processing all workers' compensation claims and providing a management information system, which has a check writing capability, for those claims.

The division has a two-year contract, which it extended for another year through June 30, 2000, to pay Firm Solutions an annual fee not to exceed $3,061,524 for processing the claims. The division also has another two-year contract to pay Firm Solutions an annual fee not to exceed $242,000 to provide the management information system. According to the division's contract administrator, as of September 27, 1999, the division has already agreed to extend the term of the management information system contract to June 30, 2000.

The City maintains two bank accounts to pay workers' compensation benefits; one bank account pays claims administered by the division and the other bank account pays claims administered by Firm Solutions. Firm Solutions is responsible for processing and issuing all of the City's checks for workers' compensation benefits. Firm Solutions is also responsible for conducting monthly bank reconciliations to ensure that the City accounts for all checks issued and cashed. The division receives the monthly bank statements for the two bank accounts and lists of canceled checks. The division then provides these documents to Firm Solutions to allow it to perform the monthly bank reconciliations.

According to the division's records, the City paid $51,310,354 in workers' compensation benefits in fiscal year 1997-98, and $43,735,244 in workers' compensation benefits for the first 9 months of fiscal year 1998-99. These payments include $2,640,065 the City paid to a managed care contractor to assist the division in determining whether the medical and hospital bills for workers' compensation benefits were reasonable.

SCOPE AND METHODOLOGY

Because individuals had cashed counterfeit checks on the City's two bank accounts used to pay workers' compensation benefits, the City Controller requested that the Audits Division conduct a review of Firm Solutions' internal controls for processing and issuing workers' compensation checks. To conduct the audit, we reviewed the applicable terms of the division's agreement with Firm Solutions. We assessed the adequacy of Firm Solutions' check security procedures and visited the facility where the company processes and mails checks. As part of our tests, we examined the monthly bank reconciliations Firm Solutions prepared for the period July 1998 through March 1999.

We did not assess whether claims adjusters approved workers' compensation claims correctly in accordance with state law. According to the deputy director of the Department of Human Resources, the department has engaged a management consultant to conduct this review in the very near future.

AUDIT RESULTS

FIRM SOLUTIONS HAS ADEQUATE CONTROLS FOR PROCESSING AND ISSUING BENEFIT CHECKS

In general, we found that Foundation Integrated Risk Management Solutions Incorporated (Firm Solutions) has adequate controls for processing and issuing workers' compensation benefit checks. After interviewing staff members at Firm Solutions to identify the internal controls used by the company, we inspected the facility where Firm Solutions processes and issues the checks. We observed that Firm Solutions stores its check writing equipment in a room that is locked electronically, and has authorized only three of its staff to have the security code to enter the room.

To issue the workers' compensation benefit checks, Firm Solutions has an automated check writer controlled by a computer. A removable-integrated circuit card contains the signature for the checks, and staff must insert this card into the check printer to issue signed checks. Firm Solutions stores the integrated circuit card in a locked cabinet within the room when the check printer is not being used. In addition, Firm Solutions also stores unused check stock in the cabinet, and only one staff member and the staff member's supervisor have keys to the cabinet.

Firm Solutions uses blank checks that have preprinted check numbers on the backs of the checks. The check stock has security features that prevents the alteration of the amount printed on each check and the duplication of the check by a photocopier. The company keeps a log recording the starting and ending numbers of the blank checks used whenever it prints checks. We examined the log and found that the starting and ending check numbers were in sequence. Further, we verified on June 21, 1999, that the preprinted check number on the next check in the check stock followed the last check number recorded in the log.

Firm Solutions' check writer also prints a different check number on the face of each check. Firm Solutions and the division uses these check numbers to record the checks the City issues and to reconcile the monthly bank statements. To control further the flow of claims payments each day, the division deposits to the two bank accounts for workers' compensation benefits only the exact amount of funds it calculates is necessary to pay the total for claims checks issued that day.

FIRM SOLUTIONS WAS LATE IN PREPARING REQUIRED MONTHLY BANK RECONCILIATIONS

Even though Firm Solutions used appropriate methods to process workers' compensation checks, the company was late in submitting to the division required monthly bank reconciliations. The division requires Firm Solutions to prepare monthly bank reconciliations within 45 days of the receipt of the bank statements for the two bank

accounts. Firm Solutions did not submit until July 15, 1999, the monthly bank reconciliations for the nine months from July 1998 through March 1999. These reconciliations arrived at the division 2 to 10 months late.

In addition, the bank reconciliations we reviewed did not show any evidence that Firm Solutions' management reviewed the reconciliations completed by its staff. For example, we observed that Firm Solutions had not resolved discrepancies identified in April 1996 and that Firm Soutions' staff identified the same discrepancies in their March 1999 bank reconciliation and needed resolution. Furthermore, because Firm Solutions was late in providing the bank reconciliatons to the division, the division could not resolve promptly problems identified in the reconciliations for the bank account administered by the division.

According to Firm Solutions' vice president for claims, the company was not able to prepare timely bank reconciliatons because it had a staff shortage and took some time to hire additional staff. In addition, according to the vice president, the division was late in sending to Firm Solutions some of the bank statements and the list of cashed checks so that Firm Solutions could perform the bank reconciliations.

Furthermore, the division delayed in requiring Firm Solutions to complete the bank reconciliations promptly. The division is responsible for reviewing the bank reconciliations performed by Firm Solutions to verify the accuracy of the reconciliations and to ensure that the City accounts for all the checks issued and cashed, as well as for all checks that remain outstanding. According to the division's senior systems accountant, the division was short of staff to review the bank reconciliations and did not formally request in writing until February 1999 that Firm Solutions complete the reconciliations due from July 1998 and after.

Because Firm Solutions and the division did not carry out their responsibilities promptly, both organizations were late in identifying some checks that had been incorrectly paid from the two bank accounts. Firm Solutions performed the bank reconciliations in June and July 1999, and Firm Solutions and the division identified almost $33,000 in checks that had been incorrectly issued or incorrectly paid from April 1996 through March 1999. For example, the reconciliations showed that the division and Firm Solutions made nine duplicate payments, totaling $5,600, to claimants and medical providers who had requested replacement checks for benefit payments they indicated they had not received. However, the bank reconciliations showed that the originally issued checks had been cashed 14 to 395 days before the division placed the stop orders, and that the replacement checks had also been cashed. We could not determine from the available records, however, who actually cashed the checks. According to the Firm Solutions' vice-president for finance, Firm Solutions was not able to verify that the initially issued checks had been cashed because his company did not receive the bank statements from the division in a timely manner. Table 1 shows the potential losses from checks that were incorrectly issued or incorrectly paid.

Table 1
Potential Losses from Improper Payment
July 1, 1998 through March 31, 1999

	Number of Checks	Firm Solutions Account	Division Account	Total
Duplicate Payments (Note a)	10	$4,174	$14,672	$18,846
Check Paid Twice by Bank	3	347	55	402
Paid in Excess of Check Amount	6	80	53	133
Returned Check	4	1,319	0	1,319
Fraudulent Checks (Note b)	16	1,251	8,997	10,248
Other Reconciling Items	5	1,927	0	1,927
Total	44	$9,098	$23,777	$32,875

Note a: Includes $13,200 that the claimant is repaying the City.
Note b: The bank already reimbursed the division for the full amount of the losses.

IMPROVING SOME ADMINISTRATIVE PRACTICES WILL HELP THE DIVISION STOP THE IMPROPER CASHING OF CHECKS

Although timely reconciliations by Firm Solutions would have quickly identified that some checks had been incorrectly paid from the City's bank accounts, some of the division's administrative practices also contributed to the claimants' ability to cash checks for which they may not have been entitled. We found that the division did not print an expiration date on the benefit checks to prevent late cashing of checks. Furthermore, the division can institute controls to prevent individuals from cashing counterfeit checks on the division's two bank accounts.

The Division Needs Additional Controls to Prevent the Late Cashing of Checks

The division made one duplicate payment to a claimant because the claimant was able to cash a check after the stop payment period expired. The division placed a stop payment request with its bank for a $13,200 check when the claimant notified the division that she had not received her workers' compensation check. The division issued to the claimant a $13,200 replacement check that she cashed. However, the claimant also received the first check for $13,200 since she also cashed that check more than six months after the division initially issued the check. She was able to cash this check because the division only stops payment on a check for a six-month period, and the claimant cashed the check a few days after the period had expired. According to the division's senior systems accountant, the division stops payment only for a six-month period because of the different fees its bank charges to stop payments on checks. To stop payment for a six-month period, the division pays a bank charge of $14 for each check the division asks the bank to not pay. To stop payment for an 18-month period would cost the division $18 per check.

The division, however, could continue to use the six-month stop payment period if it also printed a statement on each check that the check was void if not cashed within six months of the date of issuance of the check. Firm Solutions does not print a void date on the checks it issues, although the division's previous contractor did print a void date on the checks it issued for the division. According to the deputy director of the Department of Human Resources, he was not aware why Firm Solutions did not include a void date on the checks, and agreed that the checks should have a void date.

The division, through the Offices of the City Attorney and District Attorney, instituted procedures to recover the double payment from the claimant. The claimant is repaying the City at the rate of $100 each month.

The Division Can Add Controls to Prevent the Cashing of Counterfeit Checks

In January and February 1999, unidentified individuals wrote and cashed 17 counterfeit checks, totaling more than $10,000, on the division's two workers' compensation bank accounts. According to the division's senior systems accountant, the division's bank notified the division that the bank had cashed a $525.40 counterfeit check drawn on one of the division's bank accounts on January 28, 1999. He also stated that the division reviewed the bank's list of cancelled checks from January through May 1999. The division identified 16 additional counterfeit checks from January and February 1999 totaling $10,248 that had been charged to division's two bank accounts. The division notified the bank of the additional counterfeit checks. The bank reimbursed the division for the full amount of the losses because the division notified the bank within the time limit the bank sets for accepting responsibility for cashing counterfeit checks.

Although the City did not lose any funds, the division can help prevent its bank from cashing counterfeit checks by using a positive pay program for the checks the division issues. According to a bank customer service representative, under a positive-pay program, the division would provide its bank a list of the checks Firm Solutions issues, and the bank would only pay those checks on the list. If an individual presented a check that was not on the list, then the bank should not cash the check.

On June 15, 1999, the deputy director of the Department of Human Resources requested the Office of the Treasurer and Tax Collector's chief investment and cash management officer to set up a positive-pay program for its two bank accounts. According to the special assistant to the treasurer, as of August 19, 1999, the office is still processing the positive pay agreement with the division's bank.

RECOMMENDATIONS

The Workers' Compensation Division should take the following steps to reduce the possibility that the City will pay workers' compensations benefits incorrectly:

- Require Foundation Integrated Risk Management Solutions Incorporated to prepare bank reconciliations at the end of each month. Further, Firm Solutions should ensure that it resolves reconciliation discrepancies promptly by requiring a manager to review the reconciliations prepared by its staff and resolve discrepancies promptly.

- Make certain that Firm Solutions submits the bank reconciliations to the division each month. The division should review the reconciliations promptly for accuracy and resolve any reconciliation problems it identifies.

- Require Firm Solutions to print the phrase "void after six months" on all the checks it issues.

- Work with the Office of the Treasurer and Tax Collector to implement the positive pay program for the division's workers' compensation bank accounts.

We conducted this review according to generally accepted government auditing standards. We limited our review to those areas specified in the audit scope section of this report.

Staff: Elena W. Chiong, CIA, Audit Manager
Gani Soy
Wayne Chan

RESPONSE TO THE AUDIT

WORKERS' COMPENSATION DIVISION OF THE DEPARTMENT OF HUMAN RESOURCES

City and County of San Francisco

Department of Human Resources

ANDREA R. GOURDINE
HUMAN RESOURCES DIRECTOR

November 3, 1999

Mr. Edward M. Harrington
Controller
316 City Hall
1 Dr. Carlton B. Goodlett Place
San Francisco, CA 94102

Dear Mr. Harrington: **Subject: Audit Number 98101**

We have reviewed the audit report and management letter of the Workers Compensation Division's processing and issuing benefit checks.

The first two of these recommendations were implemented. Language concerning the preparation and review of bank reconciliations are reflected in the current contract with our third party administrator. The "void after six months" phrase will be printed on all checks, beginning December 1, 1999 (third recommendation). With respect to the fourth recommendation concerning implementtion of a positive pay program, a request was forwarded to the Treasurer on June 15. To date, we have not received a reply.

If you have any further questions or need additional information, please feel free to contact Fred Howell at 557-1778.

Sincerely,

Andrea R. Gourdine
Human Resources Director

Frederic A. Howell
Deputy Director of Human Resources
Workers Compensation

44 Gough Street • San Francisco, CA 94103-1233

cc: Mayor
Board of Supervisors
Civil Grand Jury
Public Library
Budget Analyst
KPMG LLP
Workers' Compensation Council